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Decision 03-05-075 May 22, 2003

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of Verizon California Inc. (U-10021-C) Petition for Arbitration with Pac-West Telecomm, Inc. (U5266-C) Pursuant to Section 252(b) of the Telecommunications Act of 1996.	Application 02-06-024 (Filed June 12, 2002)

DECISION APPROVING ARBITRATED AGREEMENT PURSUANT TO SECTION 252, SUBSECTION (e), OF THE TELECOMMUNICATIONS ACT OF 1996 (ACT)

Summary

In this decision we modify and approve the arbitrated interconnection agreement (ICA) filed by on February 18, 2003, Verizon California Inc. (Verizon) and Pac-West Telecomm, Inc. (Pac-West), under Rule 4.2 of our Revised Rules Governing Filings made Pursuant to the Telecommunications Act of 1996 (Rules), pursuant to Subsection 252(e) of the Act. We find that the ICA does not violate the requirements of Section 251 of that Act, the Federal Communications Commission's (FCC) implementing regulations therefore, or the pricing standards set forth in Subsection 252(d) of the Act. However, we do find that the Final Arbitrator's Report finding on Issue 3 of the agreement is inconsistent with Commission policy established in prior interconnection agreement (ICA) cases and therefore Issue 3 of the ICA shall be modified to comport with this decision.

Application (A.) 02-06-024 is closed.

Background and Procedural History

As required by Subsection 252(e)(1) of the Act, in this decision we approve in its entirety the proposed ICA between Verizon and Pac-West, following arbitration of certain issues the parties could not resolve through negotiation. Pac-West's previous ICA with Verizon expired on April 13, 2002.

The history of the dispute, and a complete discussion of the parties and disputed issues, are set forth in detail in the Final Arbitrator's Report (FAR), which was filed on February 10, 2003. Rule 4.2.1 required the parties to file the entire agreement conforming to the FAR, and respective statements concerning approval or rejection of the proposed ICA, within seven days after issuance of the FAR. Both parties timely filed these documents, thus placing before us the task of approving or rejecting the ICA in its current form.[1]

Rule 4.2.1 specifies that each party's statement must indicate:

a. the tests the Commission must use to measure an agreement for approval or rejection,
b. whether the party believes the agreement passes or fails each test, and
c. whether or not the agreement should be approved or rejected by the Commission.

An arbitrated ICA may be rejected by this Commission only if it does not meet the requirements of Section 251, implementing regulations prescribed by the FCC, or the pricing standards set forth in Section 252(d). This test is mirrored by our Rule 4.2.3.

[1] No comments were filed by any member of the public within ten days after the filing of the agreement, as permitted under Rule 4.2.1.

Verizon's statement urges us to take a piecemeal approach in adopting the ICA, specifically by rejecting the Arbitrator's resolution of Issues 1, 3, 4, and 7; modifying his resolution of Issues 5, 6, 8 and 18; and drafting replacement contract provisions reflecting his resolution of Issues 19 and 20, because the parties have been unable to do so themselves. Essentially, Verizon's statement reargues its position with respect to all of these issues in an effort to have the Commission overturn the arbitrated outcome on each. This is inappropriate to the task before us, which is to determine whether the ICA as a whole satisfies Section 251 and its implementing regulations, and Section 252(d) of the Act. On the issues cited by Verizon, either party's position appears lawful on its face and satisfies this standard, and we will not be placed in the position of overturning or reworking the Arbitrator's resolution of an issue, or undertaking the parties' job of translating those results into contract language.

Discussion Issue 3

We find that consistent with the outcome in a previous Commission Decision (D.) 99-09-029, and three Commission arbitration decisions based upon that rulemaking, Verizon should receive transport charges from Pac-West for Virtual NXX (VNXX) traffic pending FCC resolution of the issue in the *Intercarrier Compensation NPRM*.[2]

Issue number 3, as cast by the parties, asks whether Verizon should be allowed to collect transport charges on calls destined to Pac-West customers with disparate rating and routing points. At issue is whether Verizon should, or should not be compensated for the costs to deliver VNXX traffic to Pac-West.

[2] This ICA is approved concurrent with the Commission approval of the ICA between Pac-West and SBC-California. The VNXX issue is the same in both ICAs, although the discussion in the Pac-West and SBC-California case is more detailed.

VNXX is a form of Foreign Exchange service where the purchaser of the VNXX is not physically located in the originating callers local calling area, yet the originating call to the VNXX is considered local from the caller's perspective. VNXX traffic is interexchange traffic because it terminates outside of the originating calling area (exchange), although it is rated as a local call to the calling party. VNXX and Foreign Exchange differ from traditional local calling where the called NXX and callers NXX resides within the same local calling area.

The nature of the Pac-West's network design requires Verizon to long-haul virtually all calls to Pac-West in order for Pac-West's switch to route the call over its system to its customer. The Commission in deciding prior arbitration agreements concluded that CLECs would be absolved from paying the costs associated with transport from origination to their point of interconnection on the condition that the disparately rated and routed traffic was returned and terminated within the rate area where the local call originated.[3] For foreign exchange type of service, where the traffic does not return to the originating rate center, the Commission determined that such traffic would be subject to transport charges.[4] These policies are clearly elucidated by the Commission in D. 02-06-076;

> The calling areas adopted by the Commission govern whether a call is local or an intraLATA toll call. Any call rated as an intraLATA

[3] FCC Rule 51.703(b) forbids the ILECs from assessing any charges to transport "local" traffic, which is subject to reciprocal compensation provisions. However, Interexchange traffic is not subject to the Telecommunications Act's reciprocal compensation requirements. The California Commission determined that disparately routed, local calls and VNXX calls are subject to reciprocal compensation, not the FCC.

[4] See GNAPs Arbitration Decision 02-06-076, pp. 25-30.

> toll call under the Commission's established calling areas would constitute exchange access traffic, not local traffic. (p.20)
>
> "(W)e have no intention of making a decision in an arbitration proceeding that would have the net result of abolishing intraLATA calling. For calls that are intaLATA in nature, e.g., those beyond 16 miles, traditional access charges will apply." (p.24)

Additionally, the Commission's local compensation rules require the originating call carrier to compensate the CLEC for terminating the "local" traffic, including VNXX traffic that is disparately rated and routed, as in a foreign exchange (FX) service.

Decision 02-06-076, page 28, states;

> "…VNXX calls would be intraLATA calls, not local calls, if tied to the rate center that serves the customer. By allowing disparate rating and routing, we are allowing for those calls to become local calls, and as such, subject to reciprocal compensation. However, GNAPs is required to pay the additional transport required to get those calls where they will be considered local calls. …This is similar to the concept of the ILEC's tariffed FX service, in which the customer pays for the privilege of receiving dialtone from a different exchange. Because these calls would be intraLATA toll calls, if they were rated out of the rate center, which actually provides service to the customer, they are not subject to the provisions of Rule 703(b)."

The rationale supporting the premise of the ILEC not having to pay for transport for disparately rated and routed "local calls" was based on a quid pro quo that the CLEC bears the cost of returning the traffic from its point of interconnection to the local calling rate center. This "quid pro quo" policy promotes local competition and improves the opportunity for CLECs to utilize one point of interconnection to serve each of the rate centers within the LATA. Thus, CLECs have to balance the investment cost of adding a point of

interconnection with the cost of purchased transport, leased or otherwise, from their switching facilities to the end user.

Verizon cannot differentiate the traffic it hands off to Pac-West that is destined for the originating rate center (local NXX) from interexchange traffic destined 16 miles away from the originating rate center (VNXX). However, Pac-West knows to where it terminates the traffic it receives from Verizon. It is irrelevant whether the traffic Pac-West terminates to its customer is a voice call, or is handed off to the Internet or a private network. The rate area associated with where Pac-West delivers traffic to its customer is the relevant " termination point" for transport rating purposes. Since Pac-West knows to where it terminates traffic for its customers, Pac-West is capable of identifying the amount of traffic that is returned to the originating rate center (local NXX), and the amount of traffic it terminates which is interexchange - more than 16 miles away from the originating rate center (VNXX).[5]

We do not agree with the Arbitrator that customer location is *inmaterial* because Verizon must hand off all traffic to a Pac-West POI. Clearly, uncompensated costs are borne by the originating network provider and Pac-West's claim that a cost differential between VNXX and local NXX calls must be found is a red herring. Regardless of whether the traffic's eventual destination is the originating local NXX calling area or a VNXX destination, or an interLATA toll destination, the transport cost between Verizon and Pac-West are the same. Yet, the FAR would only allow Verizon compensation for interexchange toll calls, but not interexchange VNXX calls. We overturn the result reached by the

[5] The ICA includes non-disclosure agreements necessary to protect confidential / proprietary information.

Arbitrator on this issue, because contrary to the FAR, there is no need for Verizon to explain whether its cost of transporting traffic to Pac-West will differ based on where Pac-West delivers it. The Commission in a prior arbitration decision already addressed this issue. Decision 01-02-045, states;

> "D.99-09-029 granted Level 3 the right to assign routing and rating points and provide Virtual NXX service, so long as Pacific is fairly compensated. Pacific showed that it has uncompensated costs when carrying calls for Level 3's Virtual NXX customers. Therefore, Level 3 must compensate Pacific for the use of Pacific's facilities regardless of whether or not Pacific incurs additional costs when transporting Level 3's Virtual NXX traffic.

The prior arbitration decisions reflect a consistent Commission application of the principle of cost causation. The principle would be violated if the Commission allowed competitors to avoid paying for transport over another carrier's network in order to long haul interexchange traffic terminated in disparate rate centers. To allow such long-haul transport without transport compensation would be unfair for the ILEC, which bears the cost of its transport network. Further, such a policy in regards to VNXX, once widely adopted by the CLEC industry would potentially result in a shift in the cost of such transport to local exchange subscribers rather than to the subscribers of VNXX service which is the beneficiary of the foreign exchange like service.[6]

Pac-West has developed its VNXX product largely to serve its ISP customers, a substantial part of its business. VNXX is a valuable service that

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[6] Pac-West argues that transport charges are paid by the originating call, telephone subscriber. This may be true to a very limited extent that local exchange costs include interexchange costs within the local calling area. However, transport costs outside the local calling area are excluded. Potentially, ILECs could assign these unrecovered transport costs to local calling in any proceeding addressing local exchange costs.

subscribers are willing to pay a premium for. Such service rates should bear the costs associated with provisioning the service. Verizon offers a similar product as foreign exchange service. The FAR would have Verizon provide transport services for non-local VNXX traffic without charge to its competitors while bearing the full cost of transport for provisioning its own foreign exchange service. CLECs are free to compete utilizing wholesale services of the ILEC, other CLEC transport providers, or to provision transport services themselves.

The policies of this Commission and the Telecom Act precisely intends for carriers to invest in facilities based on the innovation incentives inherent in an openly competitive market. We refrain from creating an incentive that distorts marketplace investments by requiring incumbents to either subsidize its competitors' or shift costs to local exchange customers for inter-exchange traffic that is destined beyond the origination rate center. Such policy would encourage CLECs to become providers of termination facilities, to collect reciprocal compensation and thereby avoid investment in multiple points of interconnection, switching, and transport, and result in less network redundancy than facilities based competition economics would otherwise dictate. The competitive challenge is both on the CLECs and ILECs to invest wisely in origination and termination facilities.

Discussion Issues 2 and 17(a)

Pac-West's statement indicates its belief that the conformed ICA satisfies the rejection standard, with the exception of provisions reflecting two issues, 2 and 17(a), that were decided by the Arbitrator in the FAR. Regarding Issue 2, Pac-West is concerned that Verizon might construe the FAR to impose the FCC's reduced rate caps on presumptively ISP-bound traffic retroactively from the effective date of the new ICS. We agree with Pac-West that Paragraph 82 of the

FCC's *ISP Remand Order*[7] expressly proscribes such a result,[8] and may not be reflected in the ICA.

Regarding Issue 17(a), we also agree with Pac-West that a requirement for Pac-West to pay any allocated portion of costs on Verizon's side of the carriers' point of interconnection does not satisfy the interconnection requirements of Section 251 of the Act, and therefore must not be included in the ICA.

We have examined the conformed agreement filed by the parties, and have determined that approval should be granted, subject to the foregoing discussion. The pricing provisions comply with the standards for interconnection and network element charges, as well as the charges for transport and termination of traffic, under Section 252(d). The ICA does not discriminate against nonparties, and is consistent with the public interest, convenience and necessity, and thus comports with Section 252 (e)(2)(A). It also satisfies the requirements of Section 251 and the FCC's implementing rules, and thereby satisfies Section 252(e)(2)(B). Lastly, the agreement satisfies our own regulatory requirements.

Rule 4.2.4 requires a decision approving or rejecting an arbitrated ICA to contain written findings.[9] Consistent with this rule, we include findings in support of our order.

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[7] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Intercarrier Compensation for ISP-Bound Traffic* CC Docket Nos. 96-98 and 99-68, *Order on Remand and Report and Order*, 17 FCC Rcd 9151 (2001).

[8] "The interim compensation regime we establish here applies as carriers renegotiate expired or expiring interconnection agreements. *It does not alter existing contractual obligations, except to the extent that parties are entitled to invoke contractual change-of-law provisions."* (*Italics* supplied.) D.02-01-062 determined that the change-of-law provision in the existing ICA excludes FCC orders, and any change to the terms of the existing ICA requires a written amendment by both parties.

Comment on Draft Decision

Comments were received on April 1, 2003 from Pac-West Telecomm, Inc., Verizon California, Inc., and California ISP Association, Inc. Reply Comments were received on April 7, 2003 from Pac-West Telecomm, Inc., and Verizon California, Inc. In its comments Pac-West states that Verizon Call Origination Charges permitted by the Alternate would impose approximately $11 million of new charges on Pac-West for the same interconnections that are currently in place at current traffic volumes, and that Verizon's proposal did not include a network reconfiguration option that would avoid the imposition of Call Origination Charges.[10] The Commission recently determined in the arbitration between Pac-West and SBC-California, that the applicable TELRIC-based UNE rates should become effective January 1, 2004, and that Pac-West could avoid all such charges by reconfiguring its network with POIs located at network tandems.[11] Similarly in this case, Pac-West should have a choice to either reconfigure its network by establishing POIs at network tandems or to pay transport rates for VNXX calls. To provide Pac-West sufficient time to reconfigure its network, for purposes of this interconnection agreement, the applicable transport rates shall be effective upon January 1, 2004, on a going forward basis. We recognize the FCC could change this VNXX transport charge policy. When the FCC acts on its Intercarrier Compensation NPRM regarding

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[9] Section 252(e)(1) of the Act only requires us to include written findings as to any deficiencies in the ICA.

[10] See Comments of Pac-West Telecom, Inc., p.12.

[11] See Decision 03-05-031, p.11.

the VNXX issue, such outcome shall be reflected in this ICA via its Change in Law provision.

Assignment of Proceeding

Geoffrey F. Brown is the Assigned Commissioner and Victor D. Ryerson is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. Pac-West can identify to Verizon the amount of disparately rated and routed traffic that Pac-West terminates within 16 miles of the originating rate center in order to avoid inappropriate assessment of interexchange transport charges.

2. The Interconnection Agreement under Sections 251 and 252 of the Telecommunications Act of 1996 by and between Verizon California Inc. and Pac-West Telecomm, Inc. (ICA), filed by the parties on February 18, 2003, pursuant to Rule 4.2.1, conforms to the Final Arbitrator's Report in this proceeding, except for the modification required to reflect the resolution of Issue 17(a).

3. The pricing provisions of the ICA comply with the standards for interconnection and network element charges, and the charges for transport and termination of traffic, under Section 252(d) of the Act.

4. The ICA does not discriminate against nonparties, and is consistent with the public interest, convenience and necessity, and thus comports with Section 252 (e)(2)(A) of the Act.

5. The ICA, with the indicated modification of the outcome under Issue 17(a), satisfies the requirements of Section 251 of the Act and the FCC's implementing rules, and thereby satisfies Section 252(e)(2)(B).

6. The ICA satisfies the Commission's regulatory requirements, as reflected in its rules, decisions, and orders.

Conclusion of Law

1. Verizon is entitled to receive compensation at UNE prices for facilities used per D.99-09-029 at 32, Decision 00-08-011 at 18, and Decision 02-06-076, at 28. The UNE transport rates applicable in this order should become effective January 1, 2004.

2. It is appropriate that VNXX traffic be subject to reciprocal compensation.

3. The Commission should approve the modified ICA.

O R D E R

IT IS ORDERED that:

1. The Interconnection Agreement under Sections 251 and 252 of the Telecommunications Act of 1996 by and between Verizon California Inc. and Pac-West Telecomm, Inc., filed by the parties on February 18, 2003, is approved, subject to the modifications indicated in the body of our decision.

2. To avoid paying the costs associated with transport from origination to their point of interconnection, Pac-West shall disclose to Verizon the percentage of disparately rated and routed traffic that was returned and terminated within the rate area where the local call originated.

3. The UNE transport rates applicable in this order shall be effective upon January 1, 2004, and on a going forward basis.

4. Parties shall modify the agreement in conformance with this order and shall file it in this docket within 7 days. A copy shall be provided to the Director of the Telecommunications Division. The signed ICAs shall become effective on the date filed.

5. Application 02-06-024 is closed.

This order is effective today.

Dated May 22, 2003, at San Francisco, California.

CARL W. WOOD
GEOFFREY F. BROWN
SUSAN P. KENNEDY
Commissioners

I dissent.

/s/ MICHAEL R. PEEVEY
President

I dissent.

/s/ LORETTA M. LYNCH
Commissioner

I will file a concurrence in part and a dissent in part.

/s/ SUSAN F. KENNEDY
Commissioner

Commissioner Kennedy, concurring in part and dissenting in part,

Today's order by this Commission offers a good approach to resolving the issues before us. In particular, this order offers a reasonable resolution of the vexing problem of ensuring that virtual NXX-calls bear a fair share of the costs that they impose on the telecommunications network and on other consumers. In addition, the order provides firms that relied on previous Commission orders the time to reconfigure their networks so as to reduce the costs of transporting calls and to protect their customers from any unnecessary costs. It applies these rates for transporting virtual NXX calls prospectively, which is consistent with the FCC's delegation of authority to resolve this issue to the states. Finally, this order requires Verizon and PacWest to incorporate into their interconnection contract the reciprocal compensation prices adopted in the FCC's *ISP Remand Order*.[12] I concur in these actions.

Concerning the issue of the appropriate date for the applicability of those particular rates adopted in the FCC's *ISP Remand Order* (Issue 2 in this proceeding), this order, which sets the mailing date of today's order as the effective date, does not conform with the FCC's order. In particular, although our order cites Paragraph 82 of the FCC's *ISP Remand Order* as requiring the adoption the FCC's reciprocal compensation rates on a going-forward basis, it errs in its interpretation of this very paragraph.

An examination of Paragraph 82 shows that it does not support an extension of existing pricing terms that contravene the FCC-adopted prices and does not permit states to apply the FCC-adopted prices on a forward-going basis. Paragraph 82 states:

> 82. The interim compensation regime we establish here **applies as carriers re-negotiate expired or expiring interconnection agreements**. It does not alter existing contractual obligations, except to the extent that parties are entitled to invoke contractual change-of-law provisions. This Order does not preempt any state

[12] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Intercarrier Compensation for ISP-Bound Traffic* CC Docket Nos. 96-98 and 99-68, *Order on Remand and Report and Order*, 17 FCC Rcd 9151 (2001).

> commission decision regarding compensation for ISP-bound traffic for the period prior to the effective date of the interim regime we adopt here. Because we now exercise our authority under section 201 to determine the appropriate intercarrier compensation for ISP-bound traffic, however, state commissions will no longer have authority to address this issue. (emphasis added)[13]

As paragraph 82 clearly states, the rates adopted in the FCC's *ISP Remand Order* apply "**as**" the interconnection contract is "expiring or expired."

Although today's order rightly notes that the interconnection agreement between Verizon and Pac-West expired on April 13, 2002, it ignores the relevance of this fact to the issues at hand and fails to apply the relevant FCC regulation. First, beginning April 14, 2002 there was no contractual relationship between Verizon and Pac-West – the contract had expired. Second, since the FCC's *ISP Remand Order* and its reciprocal compensation rates became effective June 2001, there was no legal basis for this Commission to extend the reciprocal compensation rates in the "expired" interconnection agreement beyond April 14, 2002. Thus, with the expiration of the interconnection agreement, the rates contained in the FCC's *ISP Remand Order* became effective. Moreover, this Commission's extension of the reciprocal compensation prices in the expired contract is an unlawful action that both violates the pricing terms of the remand order and creates a new agreement concerning these pricing terms where none rightfully exists.[14]

For these reasons, I respectfully dissent in this order's failure to implement the pricing terms of the FCC's *IDP Remand Order* effective April 14, 2002.

/s/ SUSAN P. KENNEDY

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[13] *Ibid.*, paragraph 82.

[14] Note: As before, we distinguish the ability of states to resolve the pricing issues concerning the transport of virtual NXX calls from the issue of reciprocal compensation. On the pricing of virtual NXX calls, the FCC has not exercised its jurisdiction and the states are free to apply pricing terms prospectively.